

Message Text

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PAGE 01 TOKYO 03490 01 OF 02 031056Z
ACTION EA-12

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SOE-02 /120 W

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FM AMEMBASSY TOKYO
TO SECSTATE WASHDC 5779
INFO AMCONSUL HONG KONG
AMEMBASSY TAIPEI
USLO PEKING
AMEMBASSY MOSCOW
CINCPAC HONOLULU

C O N F I D E N T I A L SECTION 1 OF 2 TOKYO 3490

CINCPAC FOR POLAD

E.O.11652: GDS
TAGS: EEWT, ENRG, JA, CH
SUBJECT: SINO-JAPANESE LONG TERM TRADE AGREEMENT SIGNED BUT MAJOR
PROBLEMS REMAIN

REF: (A) TOKYO 2384 (B) PEKING 446 (C) 77 TOKYO 18828 (NOTAL)

BEGIN SUMMARY: SINO-JAPANESE LONG-TERM TRADE AGREEMENT (LTA)
WAS SIGNED AS SSCHEDULED BUT FINANCING AND OTHER PROBLEMS
REMAIN. CHINA RELUCTANTLY AGREED TO JAPAN'S POSITION THAT
FINANCING MUST FOLLOW OECD GUIDELINES BUT HINTED IT MAY TURN
TO OTHER SUPPLIERS. SOURCES EXPECT INTENSE COMPETITION AMONG
JAPANESE COMPANIES FOR CHINA'S BUSINESS. CHINA CAN SUPPLY
AGREED AMOUNTS OF OIL FROM PRESENT SOURCES THROUGH 1981 BUT
MUST DEVELOP OTHER SOURCES TO MEET 1982 GOAL. JAPAN MAY
BUILD NEW REFINERY TO HANDLE 1982 IMPORTS. NO MAJOR
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PAGE 02 TOKYO 03490 01 OF 02 031056Z

PROBLEMS ARE EXPECTED IN MEETING COAL EXPORT GOALS.
INFORMAL AGREEMENT WAS REACHED ON PATENTS AND IN-
DUSTRIAL PROPERTY RIGHTS BUT JAPAN WOULD LIKE FORMAL
AGREEMENT. CHINA PPEARS TO BE PLAYING JAPAN OFF AGAINST
UNNAMED EUROPEAN SUPPLIERS IN HOPES OF OBTAINING
CONCESSIONARY FINANCING AND COCOM RESTRICTED ITEMS.
END SUMMARY.

1. THE SINO-JAPANESE LONG TERM TRADE AGREEMENT (REF-TELS), WAS SIGNED ON FEBRUARY 16 AS SCHEDULED BUT FULL IMPLEMENTATION WILL DEPEND ON THE SOLUTION OF SEVERAL MAJOR PROBLEMS, PARTICULARLY THE PROBLEM OF FINANCING. EMBASSY OFFICERS RECENTLY DISCUSSED PROBLEMS CONCERNING THE LONG TERM TRADE AGREEMENT (LTA) WITH OFFICIALS AT THE MINISTRY OF FOREIGN AFFAIRS (MFA) AND THE JAPAN-CHINA ECONOMIC ASSOCIATION (JCEA).

2. WHEN ASKED ABOUT FINANCE TERMS FOR PLANT EXPORTS, JCEA SOURCE MAINTAINED THAT THE JAPANESE HAD REPEATEDLY TOLD THE CHINESE FINANCING MUST FOLLOW THE EXPORT CREDIT ARRANGEMENT AND THAT THE JAPANESE GOVERNMENT WAS ADAMANT ABOUT THIS. IN THE FINAL NEGOTIATIONS, CHINA TOLD JAPAN THEY UNDERSTOOD THIS POSITION BUT JCEA OFFICIALS COULD TELL THE CHINESE WERE NOT HAPPY ABOUT IT. THE CHINESE ASKED WHY JAPAN HAD TO FOLLOW THE CREDIT GUIDELINES WHEN SOME EUROPEAN COUNTRIES DID NOT. JCEA SOURCE COMMENTED HERE THAT WHILE THE JAPANESE SIDE DID NOT RESPOND PUBLICLY, MANY IN THE DELEGATION PRIVATELY BELIEVED WHAT THE CHINESE SAID WAS TRUE. AT ONE POINT THE CHINESE ALSO MENTIONED THAT JAPAN, IN CONSIDERING CHINA' REQUEST FOR FAVORABLE TREATMENT, CONFIDENTIAL

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PAGE 03 TOKYO 03490 01 OF 02 031056Z

SHOULD THINK ABOUT EXPORT COMPETITION SINCE CHINA WOULD ALSO BE BUYING FROM OTHER COUNTRIES.

3. JCEA SOURCE IS WORRIED THAT PRESSURE ON DEPRESSED INDUSTRIES TO GET ORDERS AND THE INTENSE COMPETITION AMONG TRADING COMPANIES MAY RESULT IN SEVERE PRICE CUTTING AND OFFERS OF WAYS TO CIRCUMVENT THE EXPORT CREDIT ARRANGEMENT. ALTHOUGH FINANCING WILL BE ON A CASE-BY-CASE BASIS, HE FEELS SOME COMMON GUIDELINES MAY BE NECESSARY TO PREVENT CUT-THROAT COMPETITION AMONG JAPANESE FIRMS AND THAT THE TIME MAY COME WHEN JAPAN AND CHINA WILL HAVE TO HOLD DISCUSSIONS TO FORMULATE RULES FOR FINANCING ACCEPTABLE TO BOTH SIDES AS WELL AS THE OECD. (SUBSEQUENT PRESS REPORTS SAY BANK OF CHINA DELEGATION WILL VISIT TOKYO MAY 15 TO DISCUSS FINANCING).

4. MFA SOURCE SAID 30-40 TRADE MISSIONS HAVE APPLIED TO VISIT CHINA AND THAT 10 PLANTS OF VARIOUS TYPES WITH A VALUE OF OVER \$11 BILLION ARE ALREADY UNDER DISCUSSION. CHINA AND JAPAN AGREED TO INCLUDE THE

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PAGE 01 TOKYO 03490 02 OF 02 031104Z
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C O N F I D E N T I A L SECTION 2 OF 2 TOKYO 3490

SHANGHAI STEEL MILL UNDER THE LTA AND NIPPON STEEL
CORP. IS NEGOTIATING FOR SEVERAL MORE PROJECTS. (ALL
SOURCES AGREE 1980 COMPLETION DATE FOR SHANGHAI
PROJECT IS IMPOSSIBLE UNLESS AS ONE SOURCE SAID:
"CHINA PLANS TO MOBILIZE 100 MILLION PEOPLE FOR THE PROJECT".)

5. OIL IS THE KEY ELEMENT OF THE LTA AND BOTH MFA
AND JCEA SOURCES SAID THAT UP THROUGH 1981 CHINA
COULD SUPPLY THE AGREED AMOUNT OF OIL FROM THE
TACHING FIELDS BUT MUST DEVELOP NEW FIELDS TO SUPPLY
15 MILLION TONS IN 1982. IN THE NEGOTIATIONS, CHINA
SAID THEY COULD SUPPLY THE ADDITIONAL AMOUNT FROM
OTHER FIELDS BUT REFUSED TO IDENTIFY THEM. THE
JAPANESE HAD TO AGREE TO THE 15 MILLION TON FIGURE
FOR 1982 SO CHINA COULD GO AHEAD WITH DEVELOPMENTS
OF NEW FIELDS.

6. JCEA OFFICIALS ADI JAPAN WOULD NEED 3-3.5 MILLIONS
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PAGE 02 TOKYO 03490 02 OF 02 031104Z

TONS OF ADDITIONAL ANNUAL CRACKING CAPACITY TO HANDLE THE PROJECTED 15 MT OF CHINESE CRUDE IN 1982. MITI IS CALLING FOR CONSTRUCTION OF A NEW REFINERY BUT INDUSTRY HAS SERIOUS DOUBTS ABOUT THE NEED AND ECONOMICS OF THE PROJECT.

7. THE FINAL LTA CALLED FOR CONSIDERABLE MORE COKING COAL EXPORTS THAN WE EXPECTED. JCEA OFFICIALS SAID THIS WAS BECAUSE THE JAPANESE HAD IDENTIFIED SUFFICIENT SOURCES OF COAL OF ABOUT THE SAME QUALITY AS AUSTRALIAN COKING COAL. ONE MAJOR PROBLEM HAD BEEN THE LOW LEVEL OF CHINESE COAL SORTING TECHNIQUES TO WHICH THE CHINESE HAD PAID LITTLE ATTENTION PREVIOUSLY (OFFERS OF JAPANESE HELP IN THIS AREA WERE REJECTED LAST YEAR). HOWEVER, A JCEA OFFICIAL BEFORE LEAVING PEKING WAS INVITED BY THE CHINESE COAL BOARD TO RETURN IN JUNE FOR AN INSPECTION OF COAL EQUIPMENT, INCLUDING A SHOWING OF THEIR NEW COAL SORTING TECHNOLOGY. WITH IMPROVED SORTING, CHINA SHOULD HAVE NO TROUBLE SUPPLYING THE COKING COAL CALLED FOR IN THE AGREEMENT ALTHOUGH INLAND TRANSPORTATION AND HANDLING FACILITIES AT THE PORTS ARE STILL PROBLEMS.

8. DESPITE THE SLOW DOWN IN THE JAPANESE STEEL INDUSTRY, JAPAN IMPORTED ABOUT 55 MILLION TONS OF COKING COAL LAST YEAR SO THE 150-300 THOUSAND TONS IN THE AGREEMENT FOR THIS YEAR CAN BE ABSORBED EASILY. THE 2 MILLION TONS SET FOR 1982 IS ABOUT 4 PERCENT OF CURRENT JAPANESE IMPORTS. NO PROBLEMS WERE FORESEEN FOR THE PROJECTED STEAM COAL IMPORTS ALTHOUGH INCREASES BEYOND THE AMOUNTS CALLED FOR IN THE FIRST FIVE YEARS WILL DEPEND ON POWER PLANT

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PAGE 03 TOKYO 03490 02 OF 02 031104Z

DEVELOPMENT IN JAPAN.

9. ANOTHER PROBLEM FACING THE JAPANESE IS THE QUESTION OF PATENTS AND INDUSTRIAL PROPERTY RIGHTS. THE DELEGATION REACHED AN INFORMAL AGREEMENT WITH THE CHINESE ON THIS QUESTION BUT IS NOT SURE THE CHINESE WILL RESPECT THEM AS PROMISED. ONE MEMBER OF THE DELEGATION TALKED WITH THE HEAD OF CHINA'S PATENT AGENCY ABOUT A FORMAL AGREEMENT BUT DIFFERENCES IN LEGAL SYSTEMS AND PHILOSOPHY TOWARD PROPERTY RIGHTS WILL PREVENT ANY AGREEMENT IN THE NEAR FUTURE, EVENTHOUGH THE JAPANESE STRONGLY DESIRE TO CONCLUDE AN AGREEMENT ON PATENTS AND INDUSTRIAL PROPERTY RIGHTS AS SOON AS POSSIBLE.

10. COMMENT: THE FINAL VERSION OF THE LTA CONTAINED NO REAL SURPRISES ALTHOUGH THERE WERE SLIGHT DIFFERENCES IN THE YEARLY OIL FIGURES AND INCLUDED CONSIDERABLY MORE COKING COAL THAN WE EXPECTED. THE CHINESE AND JAPANESE WERE ABLE TO CONCLUDE THE LTA FAIRLY SMOOTHLY BY POSTPONING THE MAJOR PROBLEMS FINANCING AND COCOM, TO A LATER DATE. IN ORDER TO IMPLEMENT THE AGREEMENT, BOTH COUNTRIES ARE GOING TO HAVE TO MAKE MAJOR EFFORTS: CHINA TO FIND SUFFICIENT OIL AND JAPAN THE FACILITIES TO HANDLE IT. FROM WHAT JCEA AND BUSINESS SOURCES HAVE TOLD US, IT APPEARS THE CHINESE ARE TRYING TO UNDERCUT THE GOJ'S SUPPORT OF THE EXPORT CREDIT ARRANGEMENT AND COCOM BY TELLING TRADE DELEGATIONS THAT EUROPEAN SUPPLIERS ARE NOT FOLLOWING EITHER ONE. WHETHER THE RECESSION RACKED JAPANESE INDUSTRIES WILL CAVE IN ON CHINESE DEMANDS FOR CONCESSIONARY FINANCING AND EXPORT OF COCOM CONTROLLED ITEMS REMAINS TO BE SEEN, BUT GIVEN THE CURRENT ECONOMIC CONDITION OF MANY INDUSTRIES, THE PRESSURE ON THEM AND TRADING COMPANIES TO DO SO WILL BE TREMENDOUS.

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PAGE 04 TOKYO 03490 02 OF 02 031104Z

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